Economic Trends

Alberta economy in transition

Alberta's economy is shifting down in the lower oil price environment. Alberta employment has shown some resiliency, but earnings continue to fall. After large declines, manufacturing and retail trade are showing signs of stabilizing at a lower level. Despite the slowdown, interprovincial migrants still flocked to Alberta in census year 2015. This month's InFocus looks at renovation spending in Alberta.

Indicator	Latest Month	Value	Change year-over-year (y/y)
Employment (thousands)	August	2,303	+1.8%
Unemployment Rate	August	6.0%	+0.8 p.p.
CPI Inflation (unadjusted)	August	1.7%	-0.9 p.p.
Retail Sales	July	$6.4 B	-3.7%
Housing Starts (annualized)	August	35,611	-19.2%
Rigs Drilling (unadjusted)	September	112	-59.7%
Manufacturing Shipments	July	$5.9 B	-14.6%
Exports (unadjusted)	July	$8.6 B	-17.3%

Source: Statistics Canada, CAODC, CMHC. p.p.= percentage points.

Household sector

Population growth slowing

As of July 1, 2015, Alberta's population was estimated to be 4,196,457, up 1.8% from a year earlier. This was the strongest growth among the provinces, but the slowest in four years (Chart 1). Net interprovincial migration was strong in the current census year, as 28,921 people moved to Alberta from the rest of Canada. Net international migration slowed significantly because of net outflows of non-permanent residents, a result of the changes in the temporary foreign worker program. Natural increase, a key population driver in Alberta, accounted for almost half of the population growth this year.

Alberta labour market holding up

Employment in Alberta has shown some resiliency, although there are signs the labour market is weakening. Employment increased by 4,700 in August following three months of declines; employment remains near December's level of 2.3 million. Public sector job gains since December (+47,900) have more than offset heavy losses in the private sector (-42,900). However, the unemployment rate stayed elevated at 6% in August and the number of job vacancies reached a new low in June. Regular employment insurance beneficiaries have increased by more than 50,000, although jobless claims have stabilized in recent months.

Average weekly earnings fall

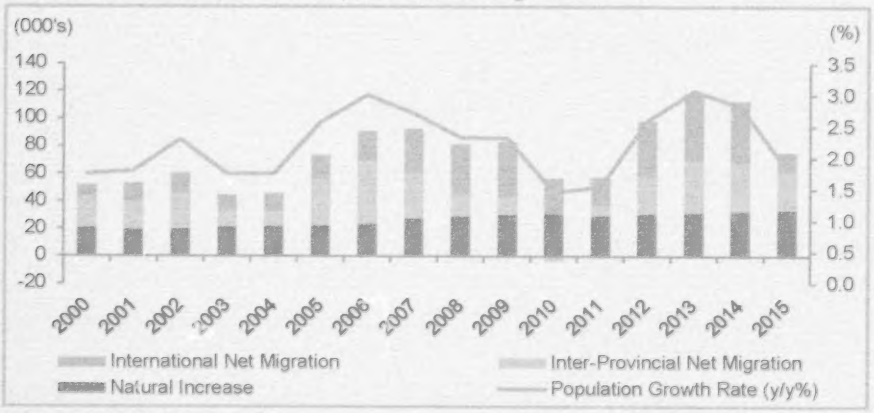
Earnings in the province are taking a hit from lower oil prices and the economic slowdown. Growth in average weekly earnings turned negative in June and July, and July posted the largest year-over-year decline in 20 years (-1.2%). Falling employment and hours worked in the high earnings goods sector are pulling down overall earnings. For the fourth month in a row in July, earnings in mining, oil and gas extraction posted a year-over-year decline. Earnings in construction have also declined in five of the seven months in 2015. Growth in earnings slowed in the service sector to a mere 0.5% y/y in July, down from an average of 3.1% in the first quarter. Accommodation and food and real-estate rental and leasing pulled down service sector earnings.

Housing activity mixed

Alberta housing starts are softening while the resale market has improved

Chart 1: Population growth in Alberta continues to moderate

Alberta annual components of population and growth



Sources: Statistics Canada

slightly. Housing starts in August declined to 35,600, the fifth y/y decline in a row. Multiple starts, which were a source of strength until July, fell 2.9% in August. Single units continued to decline, and are down 20% year-to-date (YTD). The resale market has recovered somewhat from a big correction in late 2014 and early 2015. Activity has remained fairly stable in recent months, although at a lower level compared to last year.

Retail sales steady at lower levels

Following sharp monthly declines early in the year, retail sales in Alberta stabilized at around $6.35 billion over the last few months. They still remain down 2.6% YTD. Sales in motor vehicles and parts dealers and gasoline stations pulled down overall sales. Excluding these two components, growth in retail sales has averaged over 2.5% YTD.

Alberta Business Sector

Unconventional production rising

Unconventional oil production in Alberta increased by 8.5% over the first half of 2015. The growth is attributable to production coming on-stream from recently completed oil sands projects. Conventional production, however, declined 6.5% YTD. Drilling activity in the province remains depressed. In September, the average number of rigs drilling in Alberta fell by 60% (y/y).

Exports improving

Following declines in the first five months of 2015, international exports have been increasing in recent months. Exports rose about 20% in June and July, as both energy and non-energy exports picked up (Chart 2). Exports of energy products increased by one-third, supported by higher volumes and oil prices in June and July,

Manufacturing stabilizing

After steeply declining in late 2014 and early 2015, the value of manufacturing shipments has stabilized, but remains down 11.5% year-to-date (Chart 2). Food manufacturing showed continued strength as animal slaughter increased, and chemical manufacturing shipments have risen in recent months. Buoyed by higher gasoline prices, petroleum and coal products have increased since April. Gains in these sectors, however, have been offset by continued weakness in machinery and wood products manufacturing.

Tourism gains momentum

Reflecting lower loonie and weaker economic activity, fewer Albertans are traveling abroad and more international tourists are visiting Alberta this year. International tourists increased by 1.5% YTD, led by an increase of 2.3% in non-US and 1.2% in US travelers. This reverses the trend of fewer non-US tourists visiting Alberta from 2011 to 2014. Albertans traveling abroad fell 5.5% in the first seven months of 2015, the first year-to-date decline since 2002.

Outside Alberta

China clouds global outlook

Uncertainty surrounding China's economy has increased, raising concerns about global growth and increasing volatility in global equities and commodity prices. China's manufacturing purchasing managers' index has remained below 50 since March and exports and imports have fallen. However, consumer spending has markedly improved as retail sales rose 17.8% (y/y) in August, the highest growth since mid-summer 2011. Even so, prospects for 7% annual growth in 2015 have been called into question.

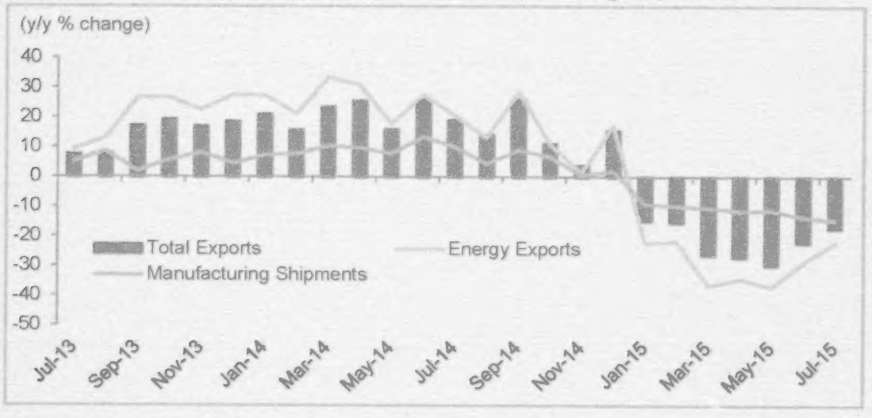
Long term interest rates decline

The recent volatility in equity markets and uncertainty in the global economy was a contributing factor in the US Federal Reserve's decision to leave its target interest rate unchanged this month. Lower inflationary pressures and the US decision not to raise rates renewed downward pressure on long-term bond yields through July and August. Yields in Canada, the US, Japan and most of the Euroarea are currently at, or near, historic lows.

US households in spending mode

Lower interest rates and prices, along with a healthier labour market, are propelling US retail sales and housing. New home sales rose over 20% in the first eight months of 2015 and existing home sales posted a 7.6% increase. Retail sales have risen by 2.3% YTD but excluding first two months of 2015, the increase is 7.4% (annualized). Supported by households, US GDP grew by 3.9% in the second quarter.

Chart 2: Declines in manufacturing shipments and exports are moderating
Alberta total exports, energy exports, and manufacturing shipments



Source: Statistics Canada

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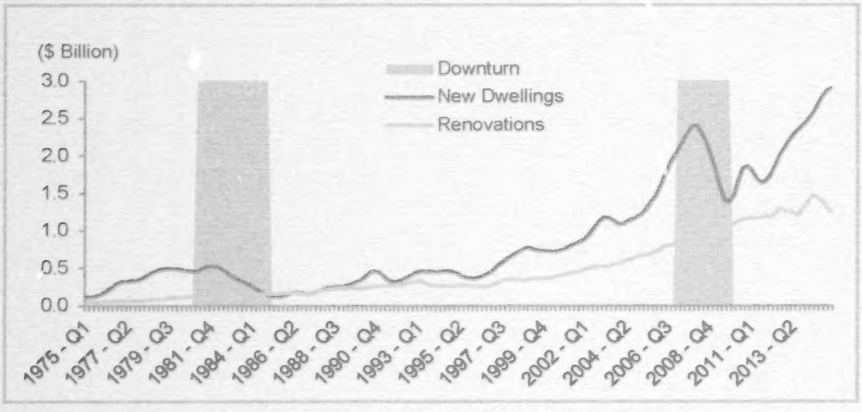
inFocus

Trends in Renovation Spending

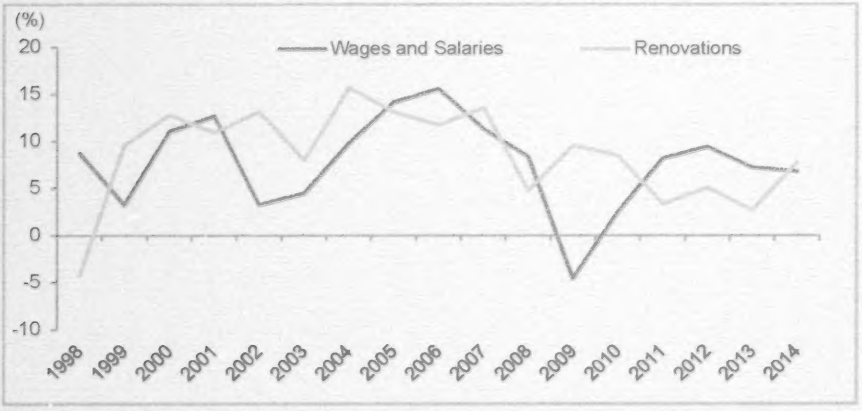
Renovations, which include structural additions, alterations, upgrades, and equipment installations, make up almost half of residential investment in Canada, but a much smaller proportion in Alberta. This is due to a greater proportion of spending going towards new dwellings. Renovation spending in Alberta has not kept pace with growth in population and incomes. However, unlike new dwellings, renovations tend to be less sensitive to economic conditions. This InFocus looks at trends in the Alberta's residential investment, specifically renovations.

Chart 1: Investment in new dwellings outpaces renovations
New dwelling and renovation investment in Alberta, four quarter moving average



Source: Statistics Canada, Alberta Treasury Board and Finance

Chart 2: Renovations have not kept pace with labour income
Year-over-year change in Alberta labour income and renovation investment



Source: Statistics Canada, Haver Analytics

Less spending on renovations

The level of renovation spending in Alberta is considerably less than new dwellings. Renovation expenditures grew 20% between 2010 and 2014 to $5.6 billion. This is compared with growth of almost 50% for spending on new dwellings, which reached $11.1 billion in 2014. In addition, after peaking in 2011, the proportion of renovation spending compared to total residential investment steadily declined to less than 30% (Chart 1). Year-to-date in 2015, renovation spending is down 18%. This is due in part to the winding down of flood related spending that kept expenditures high in late 2013 and 2014.

Strong new dwelling investment

New dwelling construction is a large component of Alberta residential investment. Strong population growth, including record high net interprovincial migration, income gains, and a tight rental market in recent years fueled the demand for housing in the province. In contrast, renovation spending has not benefited in the same way from rising incomes and population (Chart 2). Higher income households tend to spend more when they choose to renovate; however, with Alberta's high income levels, it appears households are opting to purchase new homes. As a result, less income has been spent on renovations.

National divergence

The proportion of residential spending on renovations in Alberta is significantly lower compared with the national composition (Chart 3). In addition, residential investment accounted for 6.6% of Canadian real GDP in 2013,

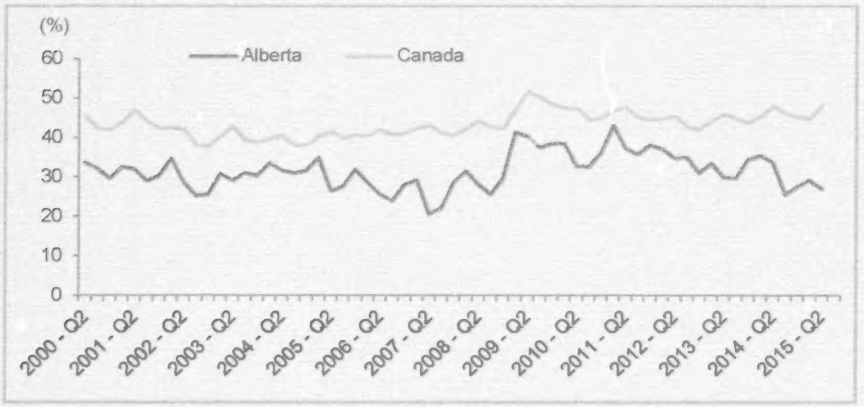
compared with 5.9% in Alberta. Most of this lower share in Alberta was due to renovations, which made up about 1.5% of Alberta GDP; in Canada, this share was about 2.5%. In contrast, Alberta investment in new housing was about 2.8% of GDP, exceeding the Canadian average of 2.5%.

The difference in spending can be partly attributed to differences in population growth (Chart 4). Over the last five years, Alberta's population increased by 10.7%, compared to the Canadian increase of 4.4%. The effect of population growth was compounded by strong income growth in Alberta compared to the rest of the country.

Alberta housing stock newer

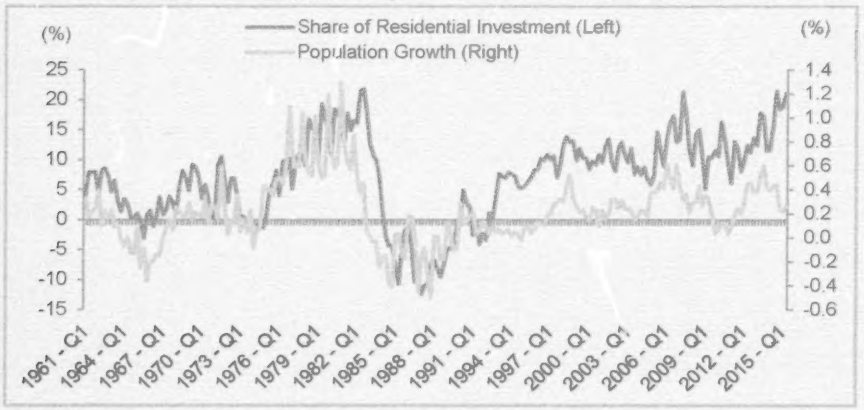
Alberta's housing stock is relatively new, which likely decreases the need for significant renovations and helps explain why more residential investment is allocated toward new dwellings. According to the Canadian Mortgage and Housing Corporation (CMHC), as of 2011, 60% of Alberta's housing stock was constructed before 1990, compared with 72% nationally. Since 2011, Alberta had strong growth in housing starts, suggesting the province's housing stock is likely newer than the 2011 estimate.

Chart 3: Renovations larger share of national residential investment
Renovations as a percent of residential investment



Source: Statistics Canada, Alberta Treasury Board and Finance

Chart 4: Population growth drives residential investment
Difference: AB and Can population growth and share of residential investment



Source: Statistics Canada, Alberta Treasury Board and Finance

Less labour for renovations

Demand for new housing and strong growth in the Alberta construction industry may have resulted in labour being allocated toward new construction, particularly in the last five years. This would result in less available labour for renovation projects, while increasing construction costs may have discouraged some households to renovate. Employment and earnings in the construction industry have started to decline, in addition to overall decreases in construction costs in recent months. This may lend support to renovation spending in the province.

Renovations less impacted by economic cycles

During previous downturns, expenditures on renovations remained stable, but new dwelling investment was scaled back (Chart 1). This suggests that renovation activity in Alberta is less sensitive to economic cycles. From 1981-1984, new dwelling investment crashed 74% and from 2007-2009 fell by 43%. However, during these same periods, renovation continued to grow increasing 6.5% and 15% respectively, the latter aided by federal tax credits.

Conclusions

Alberta residential investment is dominated by construction of new dwellings, however, renovations also make a contribution. Further, renovations tend to be less impacted by economic cycles and have remained stable during previous down-turns.

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